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"Capping Mechanism" Provision Of Massachusetts Mechanic's Lien Law Enforced

A recent case from the Supreme Judicial Court of Massachusetts holds that a subcontractor or supplier that fails to avail itself of the procedural protections provided by the Massachusetts Mechanic's Lien Law, M.G.L. c. 254, § 1, *et seq.* (the Lien Law) risks losing its lien rights entirely upon the default of the general contractor or upon the payment of all sums due the general contractor by the owner.

By way of background, the Lien Law was significantly amended in 1996. These amendments greatly expanded the potential lien claimants in various respects. In connection with increasing the number of potential lien claimants, the 1996 Amendments provided owners with additional protection from subcontractor and supplier liens. Under M.G.L. c. 254, § 4, the total value of a lien for a section 4 (subcontractor or supplier) lien claimant is limited to the amount due to the general contractor as of the date the subcontractor's notice of contract is recorded. This provides the owner with a capping mechanism so that the owner does not have to pay twice—once to the general contractor and once to the subcontractor. The subcontractor, to protect itself, should provide notice of its existence to the owner by serving it with a Notice of Identification (serving the Notice of Identification does not, however, establish a lien; the subcontractor or supplier must record and serve a Notice of Contract)[1]. By providing the Notice of Identification, the owner then has knowledge of the subcontractors and suppliers working on the project, and can account for payments by the general contractor to those subcontractors and suppliers by requiring partial lien waivers in exchange for payments. If the subcontractor fails to provide the Notice of Identification, the owner would have no knowledge of the existence of the subcontractors and suppliers, and would face the possibility of having its property subject to many liens if the general contractor had failed to pay the subcontractors and suppliers the progress payments. To protect the owner, the Lien Law caps the amount of the subcontractor's or supplier's lien at the amount due the general contractor at the time the subcontractor recorded and served its Notice of Contract. If the owner had paid the general contractor in full at the time the subcontractor recorded and served its Notice of Contract, the subcontractor's lien amount would be zero. Additionally, if the general contractor defaults and no money is due the general contractor from the owner at the time the subcontractor recorded its Notice of Contract, the subcontractor's lien amount would also be zero. Therefore, the subcontractor had a financial incentive to provide the Notice of Identification.

Over the past few years, this issue was litigated in Superior Court, with differing results. Some courts upheld the strict interpretation of the "capping mechanism," while others did not and, instead, relied upon the primary purpose of the Lien Law—namely, to provide security for those who provided labor and material to the Project. In late 2003, the SJC resolved the differences of opinion among the Superior Court decisions by holding that the strict language of M.G.L. c. 254, § 4 governs and the capping mechanism is to be enforced.[2]

In *Bloomsouth Flooring Corp. v. Boys' and Girls' Club of Taunton, Inc.*, the general contractor abandoned the project prior to Bloomsouth and another subcontractor recorded their notices of contract. Additionally, neither subcontractor served a notice of identification. The *Bloomsouth* Court expressly rejected the subcontractor's arguments that the primary purpose of the statute—security for those performing work—overrides technical statutory issues. Instead, the Court flatly stated that:

"The protection of G.L. c. 254, § 4 [the notice of identification] before [the general contractor] defaulted on the contract. Had they given notice before the [owner's] obligation to pay [the general contractor] terminated, they would have been fully protected. Their reluctance to ruffle anyone's feathers by early notification, however understandable or common in the industry, does not change the plain meaning of the statute."

The subcontractor's failure to provide the notice of identification and failure to record their notice of contract prior to the general contractor's default resulted in a lien value of zero.

In sum, this case is significant because it establishes beyond question that the "capping mechanism" provided in the Lien Law is enforceable. All participants in the construction industry—owners, lenders, general contractors, subcontractors and suppliers—should strictly abide by, and take advantage of, the procedures set forth in the Lien Law. Those who do not risk losing security for the work they performed on the project. ■

[1] *See M.G.L. c. 254, § 4.*

[2] *See Bloomsouth Flooring Corp. v. Boys' and Girls' Club of Taunton, Inc., 440 Mass. 618 (2003).*

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